1955

Clark A. Ross et al v. Producers Mutual Insurance Company et al : Brief of Plaintiffs and Appellants

Utah Supreme Court

Draper, Sandack, Draper & Oman; Attorneys for Plaintiffs;

In the Supreme Court of the State of Utah

CLARK A. ROSS, NICHOLAS G. SHAHEEN, HUGH V. BIRD, GLEN W. CROSBY, ELLIS A. SHAHEEN, OTTO L. JORGENSEN and LARRY W. BLAKE,

Plaintiffs,

vs.

PRODUCERS MUTUAL INSURANCE COMPANY, PRODUCERS FINANCE COMPANY OF UTAH, WENDEL A. DAVIS, RICHARD G. JOHNSON, ERNEST A. RICHARDS, GEORGE R. HEEDER, DAVID A. RUSSELL and NINA B. DAVIS,

Defendants.

No. 8394

Brief of Plaintiffs and Appellants

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STATEMENT OF THE CASE

Plaintiffs filed their Amended Complaint herein and later exhibits in support thereof, which show in substance as follows:

1. That certain of the persons named as Defendants in the Complaint devised a plan to establish and capitalize a Finance Company with funds to be derived from Defendant insurance company.

2. That pursuant to the plan they organized and incorporated Producers Mutual Insurance Company, as a mutual benefit association not for pecuniary profit, and Producers Finance Company of Utah under the laws of Utah.

3. That Wendel A. Davis, Richard G. Johnson, Ernest A. Richards and George R. Heeder, all of Arizona, who were the promoters of said plan, become officers and directors of both corporations, and by way of implementing the plan, they formulated,

(a) An insurance policy which they advertised on the face thereof, to be a Founders Participating Policy, being a Modified Whole Life Policy—automatically convertible annual dividends—issued by a Legal Reserve Mutual Benefit Association.

(b) A Trust Agreement between said promoters, on the one hand, and purchasers of said Founders policies on the other, in which it is represented that dividends will accrue to the policyholders on their Founders policies, which dividends they will assign to said promoters as trustees for the purpose of capitalizing a finance company with a capital of $300,000.00 taken from the insurance company by act of its Board of Directors, of which said trustees were members.

(c) An initial receipt acknowledging payment of a membership fee and a specific sum "for payment on application for

Founders Participating Policy." Over said receipt is printed an explanation of "YOUR BUILDING PLAN." This document is part of the record on appeal, marked Exhibit 12. It shows clearly the part insurance plays in said plan.

4. Said Complaint alleges that said plan is "one big operation under the simple designation of 'Producers' ". Paragraph 8, and in the remainder of the Complaint it is alleged that said plan is fraudulent and in violation of provisions of certain sections of Utah Code Annotated, 1953, to-wit: Section 31-27-15; 31-27-22; 31-19-18; 31-19-24 (2) and (3); 31-1-8; 31-9-11; 31-19-10 (3) and (4); and 31-7-7 (2) and (3). The manner in which each section is violated is alleged by reason of which said Founders Participating Policy and the Trust Agreement executed in connection therewith, are alleged to be null and void ab initio, thereby entitling Plaintiffs to return of all premiums paid on their respective policies.

5. Following said allegations each Plaintiff sets up his specific claim and prays for both specific and general relief.

II

DEFENDANTS' RESPONSE TO SAID COMPLAINT

Three separate motions were interposed to said complaint:

1. To dismiss for failure to state facts sufficient to constitute a compensible claim.

2. For a more definite statement.

3. Objection to joinder of parties defendant.

When said Motions came up for hearing only the first motion was argued.

III

The Court granted the Motion to Dismiss May 13, 1955.

IV

Plaintiffs filed a Motion, May 20, 1955, to rescind said Order of Dismissal on the following grounds:

1. That said insurance scheme was ultra vires the insurance company's charter and forbidden by 31-5-3 U.C.A. 1953.

2. That no insurance contract was expressed in the Insurance Policy, contrary to 31-19-18, U.C.A. 1953, making such policy invalid.

3. Failure to state the conditions pertaining to the insurance.

4. That the stock feature of the scheme had already been declared illegal by the Court.

5. That the policy failed to state anything about using dividends declared to policyholders to establish a finance company to be controlled by the officers of the insurance company for pay and for commissions, contrary to 31-19-18 U.C.A. 1953.

6. Writing terms into the policy which discriminate among holders of the same class, contrary to 31-27-22 U.C.A. 1953.

7. There is no contractural obligation of the Producers Mutual Insurance Co. to furnish Whole Life Insurance and premiums for such Whole Life Insurance is being wasted in unwarranted salaries, commissions, promotion and travel expense.

8. Collecting a fee for life membership for which no consideration is promised or given.

9. Failure of the Court to construe all the pleading so as to do substantial justice as required by Rule 8 (f), Utah Rules of Civil Procedure.

V

ACTION ON MOTION TO RESCIND

Hearing was had on said Motion, June 21, 1955, at which time certain exhibits in support of said motion and the Complaint were shown to counsel for Defendants with a request for an admission that they were genuine documents, to which counsel replied: "I have no objection to the genuineness of them" (R. 24).

Said exhibits were then handed to the Court informally. A lengthy argument based upon the Complaint, the exhibits and the law followed, after which said Motion to Rescind was denied, but the Court suggested that said exhibits should be formally presented and set June 29, 1955 as the time for such presentation (R. 21). On said date 34 exhibits marked for identification with numbers 1 to 34, were offered in evidence, but only 14 of them were so received, to-wit:

1 to 7 being the seven policies issued to Plaintiffs, including applications therefor, and Trust Agreements attached thereto.

12, 20, 24, 26, 31, 34 being receipts given to each Plaintiff containing an explanation of the "Plan."

33 being a photostatic copy of the Articles of Incorporation of the Insurance Company.

The remaining exhibits were rejected on the ground that they are incompetent, irrelevant and immaterial. Such rulings are challenged herein as error.

Of the 14 exhibits received in evidence only 9 are included in the record on appeal, to-wit: 1 to 7, 12 and 33. The remainder were excluded as duplications pursuant to the rules of this Court.

Of the 20 rejected, 14 are contained in the record on appeal, the remainder being excluded as duplications.

It is the position of Plaintiffs that their Amended Complaint states more than enough facts to constitute a claim upon which relief can be granted, and supported as it now is with evidence about which there is no dispute, a judgment upon the record as it stands before the Court would be in order.

B

APPELLANTS' STATEMENT OF POINTS

I

The Court erred in concluding and holding that the insurance policies mentioned in the Amended Complaint are valid

contracts, and in dismissing said Amended Complaint for that reason.

II

The Court further erred in dismissing said Complaint in the face of allegations therein which show that Plaintiffs were induced to enter into certain agreements, mentioned in the Complaint, through fraudulent representations and acts of the Defendants which would render said agreements voidable and subject to claims for damage by Plaintiffs.

III

The Court erred in striking from the record certain exhibits, listed and described in the "Designation of Record" herein, which tend to prove an illegal and void scheme out of which void, or voidable, agreements arose as alleged.

IV

The Court erred in assuming and acting upon the assumption that the issues raised by the pleadings are for the Insurance Commissioner to settle, and not for the Courts.

C

ARGUMENT

I

THE COURT ERRED IN CONCLUDING THAT THE INSURANCE POLICIES MENTIONED IN THE AMENDED COMPLAINT ARE VALID CONTRACTS, AND IN DISMISSING SAID COMPLAINTS FOR THAT REASON.

Said policies are not contracts because:

1. They lack mutuality of agreement and mutuality of obligation between the parties.

(1-a) Examination of either of Exhibits 1 to 7 (being the policies, applications therefor and the trust agreements) discloses that each of the Plaintiffs applied for a specifically numbered Founders Participating Life Insurance policy which shows on its face that it is issued by "Producers Mutual Insurance Company," a Legal Reserve Mutual Benefit Association" as an "Individual or Family Group Modified Whole Life Policy Automatically Convertible" (First page of Policy). But hidden on the second page of the policy under the irrelevant heading of "RESERVES" it is stated:

> "This policy is modified whole life, being term insurance during the first 5 years from date hereof, and at the end of such 5 year period, shall be automatically converted to whole life continuous plan on the same reserve basis * * * "

And in the last two paragraphs of the application for the policy, the following is written:

> "Do you and each of you hereby agree to exchange this policy in Producers Mutual Insurance Company for a non-assessable legal reserve life policy in the Producers Life Insurance Company after the fifth anniversary of this policy; said new legal reserve policy to be of the same face amount, at the same premium and of a Whole Life form that will contain in addition, a standard double indemnity provision for accidental death, cash surrender and other non-forfeiture benefits not offered by my present policy?"

> "I also understand that Producers Life Insurance Company will issue a policy to each individual insured and that this agreement is irrevocable."

The foregoing quotations constitute all the representations and promises of the Defendant, Producers Mutual Insurance Company, respecting the conversion of the Founders five year term policy to a whole life policy.

From said provisions it is instantly apparent that said Producers *Mutual* Insurance Company promises nothing. Neither does the Producers *Life* Insurance Company promise anything, nor is it a party to the contract.

> "A contract of insurance is not effected by a transaction which does not supply the element of mutuality of obligation, and there must be a meeting of the minds of the parties on the essential terms and elements of the contract." 29 Am. Jur. 148, Sec. 132, citing Employers' Liability, etc. vs. Frost, 48 Ariz. 402, 62 Pac. 2d 320, and Bridges vs. St. Paul J & M Ins. Co. (Neb.) 167 N. W. 64, L.R.A. 19 D 1199.

(1-b) There is also lack of mutuality of obligation with respect to the payment of a fee for a life membership in said Producers Mutual Life Insurance Company, because:

> "Each person who is holder of one or more insurance contracts issued by a domestic mutual insurer * * * is a member of the insurer, with the rights and obligations of such membership, and each insurance contract so issued shall effectively so stipulate." 31-9-11 U.C.A. 1953.

Thus, every purchaser of a policy in Producers Mutual Insurance Company automatically became a member thereof, and unless some consideration, other than insurance, was

promised or given, there is no consideration for the $5.00 fee. There is no consideration promised or given so far as anything in the policy discloses. The Trust Agreement attached to the policy (Ex. 1) together with a document delivered to each applicant on the day that he signed his application for a Founders Policy (Ex. 12) disclose that the chief benefit to come to policyholders will be stock in a Finance Company which consideration is illegal. See In the Matter of the Order to * * * Producers Mutual," 271 Pac. 2d 844, Utah Ass'n. of Life Underwriters vs. Mt. States Life Ins. Co., 58 U. 579, 200 Pac. 673.

2. Said Founders Policies (Ex's. 1-7) and the Trust Agreements attached thereto, violate the Statutes of the State of Utah and public policy and are void for that reason.

(2-a) Exhibits 12 and 19, two documents issued by the Insurance Company itself, put beyond question the fact it was engaged in selling more than life insurance, and that its plan involved an insurance policy, a trust agreement and a finance company operated together for the primary purpose of making profits. Exhibit 12 reads in part as follows:

> "PRODUCERS YOUR BUILDING PLAN.
>
> "You are buying a Founders Participating Policy with PRODUCERS MUTUAL INSURANCE CO. In addition, you are buying, or subscribing for STOCK, by signing a Trust Agreement in which dividends *earned* by you as a policy holder, and deposits made pursuant to said Trust Agreement, shall be used to capitalize and operate Producers Finance Company of Utah. Your Policy is eligible for dividends after the first policy year * * * Emphasis supplied.

"The Trustees, Wendel A. Davis, Richard G. Johnson, Ernest A. Richards and George R. Heeder * * * are directors of Producers Mutual Insurance Company and Producers Finance Company of Utah * * * ".

(2-b) That Profit and Not Insurance Protection was the very heart of the scheme is shown by the following exhibits:

Exhibit 19, being suggestions to Producer's Salesman, says in part:

"In order to show People Producer's plan, a salesman must thoroughly understand that plan himself.

"Do you know *what* we are doing?
"Do you know *why* we are doing it?
"Do you know *how* we will do it?"

"PRODUCERS *WHAT-WHY-HOW*"
"*WHAT ARE WE DOING?*

A. We are building a financial institution.

B. We are associating together approximately 4,000 policyholders.

C. We are giving you a key to:
1. Investment
2. Profit sharing and ownership
3. Security—to you while you live * * *

"*WHY ARE WE DOING IT?*

A. To improve your income

B. To mutually share in the savings and expenses of the plan.

C. To have Economic Security.

"*HOW WE WILL DO IT?*

A. Our Building Plan—Life insurance, dividends, trust fund, Finance Co.

B. Insurance companies make money.
   1. How they make it.
   2. Why we can pay dividends.

C. Finance Companies make money.

   1. Loans (a) Small loans—3% per month (How your money grows) (b) Installment buying (6% is actually about 12%)

   2. Discounts

   3. Pyramiding Capital (borrow low, lend high)

   4. Securities in lieu of return of money (Repossessions)

D. Are Finance Companies making money?
   1. Pacific Finance Company (2) Budget Finance Company (3) Seaboard Finance Co. (4) Valley National Bank.

"HOW MUCH FOR ME?

A. Premiums pay protection, earn dividends, buy you stock.

B. Services rendered earn you stock.

C. Stock pays dividends.

"WHY FOR ME?

E. It gives me all the above mentioned benefits and a policy in my own company that will build up cash values, loan values, and extended insurance privileges." Ex. 19, p. 2.

Turning back to Page 1 of said Exhibit, salesmen are told:

"This outline is very condensed. It isn't necessarily a sales talk, it is an outline. Dress it up with your personality, your ideas, and your pictures; make it a sales talk."

It may be conceded that a properly drawn life insurance contract, or a properly drawn trust agreement, or a properly organized corporation, the sole purpose of which is to make profits for its members or stockholders, may, standing alone, be perfectly legal and in harmony with public policy, but

> " * * * agreements which, though legal standing by themselves, are merely steps intended for accomplishment of an illegal object will be declared illegal. If the effect of the agreement is to accomplish an unlawful purpose, however, the agreement will be declared illegal regardless of the intention of the parties. Indeed, the mere tendency of an agreement to promote unlawful acts may render it illegal as against the policy of the law." Quoted with approval from 12 Am. Jur. Contracts pp 643-44 in Stockton Morris Plan Co. vs. Col. Tr. & Eq. Corp. 247 Pac. 2d 90, 93.

There can be no doubt, it seems to us, that the plan above as made and interpreted by the Defendants themselves, is in direct violation of the following Utah statutes:

> " * * * No such insurance company, or any officers or agent thereof * * * shall pay, allow or give * * * directly or indirectly * * * any special favor or advantage in the dividends or other benefit therein, or any paid employment or contract for services of any kind, or any valuable consideration or inducement whatever not specified in the policy contract of insurance, or give, sell or purchase, or offer to give, sell or purchase, as an inducement to the purchase of insurance, or in conjunction therewith, any stocks, bonds or other securities * * * or anything of value whatever not specified in the policy. Every officer or agent of an insurance company doing business in this state who vio-

lates any provision of this section is guilty of a misdemeanor. It shall be the duty of the commissioner upon being satisfied that any insurance company or any agent thereof * * * has violated any of the provisoins of this section, to revoke the certificate of authority of the company or agent so offending, and no certificate of authority shall be issued to such company or agent within six months from date of such revocation." 31-7-17, U.C.A. 1953.

To the same effect is Section 31-27-15, U.C.A. 1953, which provides that:

> "No insurer, * * * or other person shall, as an inducement to the purchase of insurance, *or in connection with any insurance transaction*, provide in any policy for, or offer, or promise to buy or give, or promise, or allow, in any manner whatsoever:
>
> (1) Any shares of stock or other securities issued *or at any time to be issued,* or any interest therein or right thereto; * * * (Penalty: Revocation of License. Emphasis supplied.)

Section 31-7-17, supra, forbids paying, allowing, etc. favors or advantages not specified in the policy contract, while Section 31-27-15 forbids provisions in the policy mixing up stocks, bonds and securities with insurance in any way, or the use of stocks and securities as an inducement to buy insurance under any circumstances.

The Producers Building Plan violates both sections. It is frankly stated that "we are building a financial institution through our building plan, consisting of life insurance dividends, a trust fund and a finance company, and that insurance companies make money; finance companies make money, and

that insurance dividends will "buy you stock", and finally the statement ends up with a falsehood to the effect that this plan gives "all the above mentioned benefits and a policy in my own company that will build up cash values, loan values and extended insurance privileges."

Contrary to said representations, the only policies given or promised to the Defendants herein was a 5 year term policy which expressly excludes every benefit mentioned above.

Thirty-four years ago, this Court condemned the practice of mixing stock and security deals for life insurance in accordance with Section 1167 and 1168, Comp. Laws of Utah, 1917, the substance of which sections has been reenacted in Sections 31-7-17 and 31-27-15, U.C.A. 1953. The penalties for violation of these sections were the same in 1917 as they were in 1953, to-wit: Punishment for committing a misdemeanor and revocation of the certificate of authority of the insurer. This Court quoted the 1917 law at length and then said:

> "We have quoted at length from the statute in order to show that it was the purpose and intent of the Legislature to have the business of life insurance conducted free and independent of any other matters of whatever kind or nature, and so that the person who is solicited to enter into a life insurance contract may do so entirely upon the merits of the contract of insurance presented to him. Utah Ass'n. of Life Underwriters vs. Mountain S. L. Ins. Co., 58 U 579 200 P 673, 675.
>
> "Then again it is manifest that the statute was enacted for the protection of the public and especially for the protection of those who are solicited to enter into life insurance contracts who may lack the experience and the opportunity to guard themselves against

the wiles of the experienced insurance solicitor." Ibid, 200 Pac. 677.

> "After a careful consideration of all the evidence, and especially the documentary evidence which is not and cannot be contradicted or explained, we are all agreed that the plan pursued by the Company in taking subscriptions for stock in connection with contracts of insurance is clearly violative of the provisions of our statutes, and if permitted by this Court would soon lead back to the very practices in writing life insurance which the statute, we think wisely prohibits." Ibid 200 Pac. 677. (Emphasis supplied.)

Note that it was the "plan" in the foregoing case that was condemned and held to be illegal and not just a single step in the plan. This is logical, equitable, wise and in full accord with legislative intent, and applies with full force against "the plan" of the Defendants herein. It violates both sections of the 1953 Insurance Code, to-wit: Sections 31-7-17 and 31-27-15, U.C.A. 1953, supra.

The penalty for violation of these sections is plain and unambiguous. Violation of the first constitutes a misdemeanor, punishable as such, and revocation of the authority of the insurerer to do business in the State. It *shall be the duty* of the Commissioner to revoke.

With respect to the second, the Commissioner may revoke the license of the insurer for violation thereof. The Commissioner, though satisfied that the Defendant insurer company herein was engaged in a plan of offering and selling insurance and securities together, did not invoke the penalty provided by the statute but was content to issue an order restraining the company "from selling, offering or promising to give,

or allowing in any manner whatsoever any shares of stock or other securities issued or at any time to be issued or any rights therein in connection with or as an inducement to the purchase of any insurance or insurance type benefit." See In the Matter of the Order Issued to American Buyers Insurance Company and Producers Mutual Insurance Company, a Utah corporation. 271 Pac. 2d 844.

Said order may have stopped such sales as to future prospects, but it gave no remedy or redress whatever to these Plaintiffs and about 4,000 other holders of Founders Policies; indeed, as the evidence will show, it has permitted the same practice to continue as to them, which this Court said, in the above case, the statute wisely prohibits.

When the matter came before this Court, nothing was presented for determination except the question as to whether Section 31-27-15 is applicable to mutual benefit associations, and with respect to that the Court held that the "context clearly indicates applicability to such association," and accordingly it sustained the cease and desist order of the Commissioner.

The only purpose in reciting the foregoing history, and other matters to follow, is to show that these Plaintiffs have been and are the victims of an illegal scheme which is void, and by reason thereof they are entitled to the return of all funds paid into it. This, of course, is in addition to the claim that no contracts exist between Plaintiff and the insurance company for want of mutual agreement and obligation and lack of, or failure of, consideration.

3. *Additional Proofs of Illegality.*

(a) The injunctive order of the Commissioner was dated September 4, 1953, as shown by the record in this case, but "the plan" was pushed vigorously with respect to every applicant who had signed an application before September 4, 1953, and as to every holder of a lapsed policy and to every holder of a Founders policy to prevent its lapse.

(a-1) Under date of September 11, 1953, the Defendant insurance company, by its President, Wendel A. Davis, wrote to the members of said company as follows:

> "Dear Member:
>
> "In reporting to you about your benefit-association, it gives me a great deal of pride to look back the past three years and see the PHENOMENAL growth of your company. Producers was organized just three years ago. * * * When you joined your association, you received your insurance policy, but, in addition to the insurance, you are entitled to other privileges. You will also be one of the ORIGINAL stock-holders of Producers Finance Company of Utah." Par. 1, Ex. 29.
>
> " * * * we expect to have your finance company off to a good start. We wish we had a million dollars to loan at the start, for the outlook is so great that we can not help but feel that we could place it in a short time, but as we grow and more dividends are paid, and we pyramid the capital, we will increase the worth and value of your company." Par. 2, Ex. 29.
>
> "Now, some of those same CHARACTERS * * * have, because of a technicality, tried to have our plan of selling stock with insurance declared illegal. We are going to let the Courts decide, but regardless, we have built our finance company. AND REMEMBER

THIS—we have a new program that will be even better than the last, * * *" Last Paragraph, Exhibit 29.

(a-2) Then under date of December 1, 1953, about two months after the District Court of Salt Lake City had affirmed the Insurance Commissioner's action, Mr. David A. Russell, as Vice President and Secretary of Producers Mutual Insurance Company, advised policyholders as follows:

> "NOW HERE IS THE BEST NEWS OF ALL! THOSE OF YOU WHO HOLD TRUST CERTIFICATES OBTAINED THROUGH DIVIDENDS, CONTRIBUTIONS TO THE TRUST FUND FROM YOUR POLICY, OR CERTIFICATES OF EVIDENCE TO THE TRUST FUND FOR RECOMMENDING NEW POLICYHOLDERS, CAN NOW EXCHANGE THESE CERTIFICATES FOR STOCK * * * "
>
> "Although your Finance Company is now open and the initial stock issued, there will continue to be future issues as dividends from your policies are declared and become available for deposit to the trust fund. Those of you who have not yet received dividends may look forward to receiving dividends as your policies become eligible. * * * DON'T LET YOUR POLICY LAPSE, AS IT IS THE ONLY MEANS BY WHICH YOU CAN OBTAIN ADDITIONAL SHARES OF THE ORIGINAL STOCK AUTHORIZED BY THE TRUST AGREEMENT."
>
> "We are sure that the beginning of Producers Finance Company is what you have been hoping for and eagerly awaiting for a long time. It is the fulfillment of a plan and goal started only three short years ago * * * "Exhibit 30, Pars. 2, 4 and 5.

(a-3) At the beginning of the next year, January 22, 1954, a remarkable letter was written to Hugh V. Bird, a Plaintiff

herein, which shows that certain service stations (gas and oil) "are members of your Producers Companies and are some of the visible evidence of the accomplishments of the Program of which you are a member. They are one of the major sources of business for the Finance Company in which you are to receive stock. * * * Your policy has been in a state of lapse for a few months * * * lapse will have no effect on your receiving dividends * * * This dividend will be * * * 30% of your annual premium as expected and will be paid in capital stock in the * * * operating Finance Company, if you will * * * keep your program in force * * * ". Exhibit 27.

This is a clear admission of the indivisibility of the Producers Companies; the bait of high dividends and Finance Company stock as an inducement to pay more insurance premiums. This is clearly illegal.

Section 31-27-15, supra, prohibits the use of any agreement or understanding whatever, promising profits, etc. "in connection with any *insurance transactions.*" And Section 31-1-11 states that "Insurance transaction" includes "transaction of matters subsequent to execution of the contract and arising out of it."

(a-4) Following the foregoing, under date of February 15, 1954, a report was made by Producers (not by Producers Mutual Insurance Company alone) to members of Producers, which announces and represents that: (See Exhibit 28, last document therein)

> 1. "The declaration of a 30% dividend for the year 1953, payable to all policies in force which were issued in 1952 or prior years." (First Paragraph).

2. "That your company has been able to pay a 30% dividend for the past three years out of its profits to capitalize a Finance Company." (Third paragraph.)

3. " * * * the Company has gone all out to obtain top quality sales personnel and to recruit members who are building a future with the Company." (Fifth paragraph.)

4. " * * * that to continue to participate in the valuable stock and insurance benefits, your policy must remain in force. If your policy has become lapsed for one reason or another, we invite you to strongly consider the advisability of reinstating while you may still do so." (Sixth paragraph.)

5. "The Producers Finance Company w h i c h has been capitalized through the savings from your life insurance policy is well on its way now." (Page 3, first paragraph.)

6. "Because of the tremendous possibilities and highly profitiable nature of the service station and merchant discount business, it was decided by the management of your company to devote a major portion of its efforts and funds available to this business. * * * The stockholders of Producers Finance Co. are also owners of Producers Credit Service." (Page 3, para. 3).

7. " * * * The extent to which we can get behind this program and patronize the dealers who have our service, will largely determine the profits it makes for us." (Last page, 3rd paragraph.)

The foregoing exhibits mentioned in Paragraphs a-1 to a-4 above confirm the nature and unity of the scheme or program described in Exhibit 19 above, and shows the same to be flagrantly against the law, both in its inception and as now being carried on.

4. *Proofs of Other Types of Illegality.*

(a) It is unlawful to discriminate among policyholders of the same class. Section 31-27-22, U.C.A. 1953.

(a-1) In the application contained in Exhibit 1, Plaintiff, Larry W. Blake, refused to agree that policy applied for would not take effect until issued by the home office; he refused to allow inspection of records made concerning him by any doctor; and finally he refused to agree to exchange his policy in Producers Mutual for one in Producers Life, nevertheless he was sold a Founders Policy for $6,000.00 coverage.

All other Plaintiffs agreed to just the opposite and all of them were sold Founders Policies.

From 1951 to sometime in 1953, all Founders Policies provided for exchange of the Founders Policy for one in Producers Life Insurance Company—the State in which it was organized is not disclosed, if it had any existence at all—but later, August 17, 1953, one Arnold J. Hendrickson signed an application which provided that his policy should be exchanged for one "in a Utah legal reserve insurance company" subsequent to the authorization of said company "to make contracts of life insurance," which date, of course, might never arrive.

(a-2) Section 31-13-24 provides that "an insurer may loan its funds upon the pledge of securities or evidences of debt eligible for investment under this chapter." Exhibit 12 shows that on June 12, 1953, Larry W. Blake paid the insurer $612.20 for a paid-up 5 year term Founders Policy. Exhibit 13 shows said Blake depositing $485.76 in the Pro-

ducers Finance Company, being equal to four annual premiums on his Founders Policy, from which Producers agrees to pay annual premiums on said Founders Policy for four consecutive years, and to pay Blake 3% annually on the balances held by the Finance Company. Any way you look at this transaction it makes no sense other than that it is a juggling of insurance premiums between the Insurance Company and the Finance Company, for which there is no warrant in law.

(a-3) Section 31-7-12, U.C.A., 1953, provides that:

> "No person having any authority in the investment or disposition of the funds of a domestic insurer * * * shall be the beneficiary of any fee * * * or other emolument because of any investment, loan, deposit * * or exchange made by or for the insurer, or be pecuniarily therein in any capacity."

Every feature of the Program in this case has its beginning in money taken out of the insurance company by its directors, and contrary to the above statute some of said directors are enabled, by contract, to take fees and emoluments therefrom in the trust fund (See Trust Agreement in Exhibit 1) and as directors of the Finance Company they are enabled to take another bite out of the dividends that reaches it.

(a-4) Section 31-19-18 provides that:

> "No insurer * * * shall make any contract of insurance or agreement as to such contract, other than is plainly expressed in the policy issued thereon. Any such understanding or agreement not so expressed shall be invalid."

Section 31-19-11 provides that:

(1) "The written instrument, in which a contract of

insurance is set forth is the policy," and (2) "a policy shall specify (g) the conditions pertaining to the insurance."

Not a word appears in the policy about using the premiums collected by the insurance company to build an outside financial institution, nor is any clear plan, nor binding agreement, written into the policy for whole life insurance. Therefore, any provisions in the policy relating to whole life insurance, together with all the provisions of the Trust Agreement are invalid.

(a-5) Section 31-19-24 provides:

> "(2) No person shall wilfully collect as premium for insurance any sum in excess of the amount actually expended or in due course is to be expended for insurance applicable to the subject on account of which the premium was collected.
>
> "(3) The excess collected shall be returned to the person entitled thereto within a reasonable length of time.
>
> "(4) Each violation of this section shall constitute a misdemeanor."

Reference to Exhibit 4, the Founders Policy of Plaintiff, Glen W. Crosby, age 45, shows that his annual premium for insurance coverage of $10,000.00 is $349.90, or $39.49 per thousand. This apparently was meant to be the annual premium for whole life insurance; but as already shown, the Founders Policy is merely a five year term policy and there is no binding provision for whole life, thus it appears that Mr. Crosby paid $39.49 per thousand annually for mere term insurance.

Reference to the rates charged by an old line insurance company, chosen at random, Page 406, Little Gem Life Chart for 1954, shows that said company's rate for whole life (ordinary life) insurance at age 45, is $39.37 per thousand and its rate for five year term at the same age is $11.76, so by that standard Producers Mutual herein charged more than 3 1-3 times more than the normal cost of five year term insurance such as it sold these Plaintiffs, and it has returned none of said excess to any of these Plaintiffs, except a partial return to Plaintiffs, Clark A. Ross and Nicholas G. Shaheen. (See Transcript of Proceedings, Page 21.)

On the contrary, of $1,007,035.78 in receipts collected by said insurer, $830,438.86 had been spent as of December 31, 1954, as shown by the annual reports of said insurer to the Insurance Commissioner of Utah, copies of which are part of the Record on Appeal herein, marked Exhibits 8-11. A compilation of receipts and disbursements from said reports shows the following:

RECEIPTS

1950	Three month operation, Bal.	$ 5,616.74
1951		44,573.15
1952		191,377.81
1953		346,928.94
1954		418,539.14
	Total	$1,007,035.78

Receipts compiled from Exhibits 8, 9, 10 and 11, Line 2, Page 2 of each exhibit

DISBURSEMENTS

1951	$ 35,228.96	
1952	148,788.12	
1953	302,848.85	
1954	434,572.92	
		830,438.86
Balance	$	176,596.92

Disbursements compiled from line 22,
Page 3 of each exhibit.

A simple calculation shows that approximately 83% of its receipts over the period accounted for was spent and only approximately 17% was saved.

The breakdown of the huge expenditures tells a story as follows:

Net Death Claims Paid—From line 9, Exhibits 8-11

1951	$ 6,000.00
1952	3,400.00
1953	6,600.00
1954	26,000.00
Total	$ 42,000.00

Dividends Paid—From line 17, Exhibits 8-11

1951	None	
1952	None	
1953	$14,769.27 paid in cash	
1954	51,879.43 paid in cash	
Total paid to policy holders		$ 93,879.43

Salaries and Travel Expenses paid to officers and trustees
From lines 25 and 27, Page 3, Exhibits 8-11

1951	.....	$ 486.67
1952	.....	14,339.65
1953	.....	36,909.31
1954	.....	51,851.23
Total	.....	103,586.86

of which $38,384.82 was travel expense of officers.

Salaries to Office Employees—From line 22, Page 3, Exhibits 8-11

1951	.....	None
1952	.....	$ 12,145.00
1953	.....	36,600.63
1954	.....	39,079.53
Total	.....	$ 87,824.16

Commissions paid to Officers, Agents and Employees:
From lines 13-14, Exhibits 8-11

1951	.....	$ 23,316.89 Lines 13 and 14
1952	.....	102,575.68
1953	.....	162,688.46
1954	.....	110,504.50
Total	.....	$399,085.53

Travel Expense, Managers and Agents: Line 27, Page 3

1951	.....	$ 195.39
1952	.....	1,269.39
1953	.....	290.11
1954	.....	1,666.65
Total	.....	$ 3,405.54

Agency Meeting Expense: Line 36

1951	$	310,00
1952		1,569.30
1953		1,776.68
1954		675.96
Total	$	4,341.94

Medical and Inspection Expense: Line 38

1951	$	657.80
1952		4,030.15
1953		9,401.13
1954		2,137.65
Total	$	16,226.73

Legal, Accounting and Actuarial Expenses: Lines 34 and 37

1951		None
1952	$	780.00
1953		3,344.49
1954		5,530.26
Total	$	9,654.75

Grand Total to Personnel	$624,125.51
All other Expenditures	112,433.92
Grand Total Expenditures	$830,438.86

From the foregoing it is obvious that about 73% of all funds spent went to officers, agents and employees of the insurance company, while only about 11% was paid in benefits to policyholders.

At the end of 1954 there were only 2970 policyholders in the company covered by $14,154,492.00 of insurance. (See

Ex. 11, p. 9). To write and keep those policies alive the company spent $736,559.43, or approximately $250.00 per policy. This great sum includes no taxes as the company was exempted therefrom on the theory that it is a Mutual Benefit Association.

As a Mutual Benefit Association the members owned every dollar in the company, subject only to the payment of reasonable overhead and expenses of doing business.

Section 31-7-10, entitled "Unlawful payment of salaries, compensation or pensions to officers, directors or employees," provides that no such payments shall be made unless authorized by the Board of Directors, and representing compensation in reasonable amount for services actually rendered * * * " U.C.A. 1953.

In the face of this statement, a contract was entered into with one William A. Parr of Phoenix, Arizona, whereby he became Regional Sales Manager of the Insurance Company, when said Company has at no time been authorized to do business outside the State of Utah. (See Exhibits 8, 9, 10 and 11, Page 8, Question and Answer 29).

In common parlance, when Region and State are used in the same context, Region means a territory larger than a State, but the Producers Mutual Insurance Company had no authority to operate outside the State of Utah, and as it was at all times fully staffed with a State Sales Manager and six District Managers under him, all receiving high pay (See Exhibits 8 to 11, Schedule G last page) no reason seems to exist why Mr. Parr should have been employed as a sales manager under any name, yet he was, and he was paid therefor as follows: 1952,

$14,817.25; 1953, $14,093.40; 1954, $11,455.88, Total $42,-366.50, which is more than the company paid out in death claims in four years. (See Schedule "G," last page of Exhibits 9, 10 and 11.)

Equally unexplained and unjustified are salaries paid to three resigned Regional Officers of Mesa, Arizona, for the year 1953, as follows:

Vice President — Richard G. Johnson	$ 9,364.00
Treasurer — George R. Heeder	9,364.00
Secretary — Ernest A. Richards	9,364.00
Total	$28,092.00

These salaries were paid as of December 31, 1953 (See Exhibit 10, Schedule "G," last page).

On the front page of the same exhibit for the year ended December 31, 1953, David A. Russell is shown to have been both Secretary and Treasurer, and Schedule "G" shows that he received a salary of $6,000.00 for his services. If Russell acted as both Secretary and Treasurer in 1953, then the payments to Heeder and Richards cannot be justified.

It may be noted also in Schedule "G," that President Wendel A. Davis got a salary of only $7,500.00 in 1953, while Vice President Richard G. Johnson got $9,364.00, which is not justified by any fact stated in the report. Indeed, nothing appears in the record to justify total payments to an average of 14 top officers and salesmen who were paid a total of $388,-799.15 in the years 1952, 1953 and 1954 (See said Schedule "G", on these years). The total receipts for these three years was $956,845.89, and 40% thereof went into the pockets of

said top people. In addition they rode around in an automobile and airplane owned by the Insurance Company.

There is no record of the purchase of these vehicles in the reports to the Commissioner, but in Exhibit 10, page 3, line 42(d) $600.00 is taken for depreciation on an automobile, while in Exhibit 11, page 4, line 43, ownership of a Company airplane is listed as a non-admitted asset.

How did they get that kind of money to spend so lavishly from term insurance policies? The answer is that they collected $1,007,000.00 on term insurance that should have cost about $250,000.00, because they collected premiums for whole life insurance that turned out to be only term, as shown above.

From the foregoing it is obvious that $750,000.00 was excess premiums and should have been assigned to surplus and apportioned and paid to policyholders as required by law.

It seems, however, that Managers of the "Program" felt that the return of 30% of four annual premiums met the requirements of the dividend clause of the Founders policy, and that all other surplus could be disposed of by them as they chose. Attention has already been called to the fact that policyholders were advised in the application which they signed that the Founders policy had no cash surrender values and no other non-forfeiture benefits.

(a-6) The Charter of Producers Mutual Insurance Company states its purpose is to form "a mutual benefit insurance company *not for pecuniary profit.*" (Ex. 33, preamble page 1. Emphasis supplied.)

" * * * and generally to conduct a mutual benefit

association in all its phases under the provisions of the Insurance Laws of the State of Utah * * * ". Ibid page 2, para. IV.

On the theory that mutual benefit companies make no profits, the State exempts them from taxation, (Section 31-14-4 (1) and Producers Mutual has had the benefit of this exemption in spite of the fact that the evidence shows that the primary object of Producers "Program" is to make profit.

One of the four basic requirements to the holding of a certificate of authority to write insurance in Utah is that only such insurance shall be done as is authorized by the insurer's charter (Sec. 31-5-3 (3) U.C.A. 1953).

The conclusion appears to be inescapable that said Founders Contracts are invalid and void for lack of mutuality, failure of consideration and illegality, for which reason the Complaint of the Plaintiffs should not have been dismissed.

II

The Court further erred in dismissing said Complaint in face of allegations of the Complaint and the undisputable evidence in support thereof.

1. Allegation 4 of the Complaint and the proof presented above not only shows that the whole Program is illegal, and against public policy and void, but it also presents facts sufficient to support a claim for damages based on fraud and deceit. Further examples would merely be cumulative. (See Fountain vs. Folsom, 336 U.S. 681, 93 L. Ed. 972).

III

The Court erred in striking from the record Exhibits 8 to 11, 13, 14, 17, 19, 22, 25, 27, 28, 29, and 30, being a part of the Record on Appeal herein, which tend to prove an illegal and void scheme out of which void or voidable agreements arose as alleged, for the following reasons:

(A) They fully met the requirements for admissability in evidence as stated by counsel for Defendants in his stated objection to their admission:

> "I therefore object, Your Honor, to all Exhibits which have been offered, except those which had to do with the sale of the policy itself, the contract of insurance, the application, the trust agreement, anything that went into the sale of the policy was not objected to." (Transcript of Proceedings, R. 24).

(B) Every exhibit which was rejected was, in modern slang, a "sales pitch," except the annual reports to the Insurance Commissioner (Ex's. 8 to 11 inc.)

(C) It will be borne in mind that selling of new policies, holding those already sold, and re-selling those that had lapsed was a continuous process. Every policyholder was expected to be a salesman as shown in many of said exhibits, and therefore nearly all letters to members seek their cooperation in selling the "Program" which is readily shown as follows:

> (1) "WHY FOR ME? A. Get benefit of many thousand persons directly and indirectly associated with Producers. 1. They will help my Company build. 2. They will have their friends use our company and I will profit from that." (Ex. 19, par. V.)

(2) The second paragraph of Exhibit 22, shows that policyholders have been paid for recommending new policyholders, and in the last paragraph of said Exhibit it is stated:

> (2) "The future of your company depends to a large extent upon you. * * * However, it will be through the continued efforts and loyal support of your present and future stockholders that your company can reach the maximum heights attainable."
>
> (3) "Producers Mutual Insurance Company has made the rapid growth and strides that it has through your faith and cooperation, and because of that faith and cooperation many of you brought into existence the Finance Company * * * ."
>
> "It wasn't the 'Doubting Thomas' that built the Producers Mutual Insurance Company and Finance Company. It was you loyal faithful policyholders." (Exhibit 25, Par's 4 and 6).
>
> (4) Exhibit 21 is a whole letter devoted to reselling a policy to a lapsed member.
>
> (5) "You must remember that you are the members and the stockholders of Producers. This is a cooperative effort. If you want to assure the success of your enterprises you can do so by encouraging your friends to use the facilities of Producers Credit Service." (Letter to members, January 3, Exhibit 28.)

In the same Exhibit 28, a report to members is attached under the simple caption of "Producers." It boasts in capital letters of having been able to pay a dividend of 30% out of profits "for the past three years" and calls attention to a chart on the next page of the report to prove that the program has been operated to the best interest of members. Members are then admonished to

"REMEMBER THAT TO CONTINUE TO PARTICIPATE IN THE VALUABLE STOCK AND INSURANCE BENEFITS YOUR POLICY MUST REMAIN IN FORCE."

The chart on the next page is remarkable for what it does not show. It shows growth in ledger assets of $5,616.74 as of December 31, 1950, to $101,634.07 as of December 31, 1953, but what it does not show is that $101,634.07 is all that was left of $588,496.64 collected by the Insurance Company over that period as shown by the reports made to the Insurance Commissioner, and analyzed above. This is what makes said rejected exhibits so competent, material and relevant as evidence herein.

Again, the boast that a 30% dividend has been paid out of profits is highly deceptive. Any ordinary person would construe "profits" to mean gains or earnings made by the Company's wise investments, and

> "The understanding of an ordinary person is the standard used in construing a contract of insurance, and ambiguity in language must be construed against the insurer." Arenson v. Nat'l Auto Casualty Co., 286 Pac. 2d (Cal.) 816. Decided August 15, 1955.

The only earnings made by the Company's investments during the period was $477.99 as shown in lines 24 to 29 of Exhibits 8 through 10, so it appears beyond question that the so-called dividend was only a partial return of the policyholders own premiums, beginning at the end of the second policy year.

6. Exhibit 29 is a good illustration of double talk. It

is a report to members a week after the Insurance Commissioner enjoined the sale of stock with Founders policies. After lauding the "PHENOMENAL growth of your Company" it goes on to say:

> "PLEASE TAKE NOTE OF THIS: As of September 1, 1953, the management of your association CLOSED the sale of the Trust Agreement * * * . It means that all the ORIGINAL stock has been subscribed for * * * ." (Paragraph one.)
>
> "Now some of those same CHARACTERS * * * have because of a technicality, tried to have our plan of selling stock with insurance declared illegal. We are going to let the Court decide, but regardless, we have built our finance company." (Last paragraph.)

Then follows a boost for a new program. It is pretty obvious why they closed the sale of Founders policies and Trust Agreements.

7. Three months later, as shown by Exhibit 30, a vigorous effort was being made to keep the insurance and stock program alive:

> "DON'T LET YOUR POLICY LAPSE, AS IT IS THE ONLY MEANS BY WHICH YOU CAN OBTAIN ADDITIONAL SHARES OF THE ORIGINAL STOCK AUTHORIZED BY THE TRUST AGREEMENT." (Paragraph 4.)

IV

THE COURT ERRED IN ASSUMING AND ACTING UPON THE ASSUMPTION THAT THE ISSUES RAISED BY THE PLEADINGS ARE FOR THE INSURANCE COMMISSIONER TO SETTLE AND NOT FOR THE COURT.

1. The Department of Business Regulation, through its Insurance and Securities Commissioners, initially passed upon and approved the Producers Mutual Insurance Company's Charter, its Founders policy and the Trust Agreement providing for the sale of stock with said policy.

Later said Department became convinced that dealing with securities in connection with insurance was in violation of Section 31-27-15, U.C.A. 1953, and it should have known that such practice is also prohibited by Section 31-7-17.

The penalty for violation of both of these sections is revocation of the certificate of authority of the offender to do business and no petition for reinstatement may be granted in less than six months after revocation.

The reason for thus suspending authority would seem to be to give the Insurance Commissioner an opportunity to protect the rights of policyholders to whom policies have been unlawfully sold, and to give the insurer a chance to purge itself and to have its authority to do business in accordance with law, renewed, as held by the Court in the Utah Ass'n of Underwriters case, supra, 200 Pac. 673, 678.

But the Commissioner, acting through the Department of Business Regulation, became satisfied that the Defendant insurance company was acting in violation of law, elected to proceed against it under Section 31-27-15, U.C.A. 1953. (The statute relied upon by the Commission in entering the order and by the lower Court in affirming that order is U.C.A. 31-27-15. See "In the Matter of the Order, etc," supra, 271 Pac. 2d 844.

The Commission, however, for reasons not stated, did not invoke the remedy provided in that section, nor in Section 31-7-17, but it did apply the remedy of injunction provided in Section 31-27-2 for engaging in acts or practice to control rates; unfair discrimination, or for creating a condition detrimental to free competition, which remedy is wholly inadequate for vioaltion of Section 31-27-15, and has resulted in leaving all holders of Founders policies with but two choices: First, to lapse their policies and lose premiums already paid, or second, continue to pay excessive premiums to keep an illegal scheme alive.

In view of this situation it would be useless to seek further administrative relief.

2. Our Courts have jurisdiction to declare all agreements to have no force as contracts, especially when it so appears on the face of such agreements and to grant relief thereon.

> 3. "An erroneous construction of a statute by the State Insurance Department cannot confer upon the insurance company a fixed right to issue a form of policy unauthorized by the statute * * * when a right to do a thing depends upon legislative authority, and the legislature has failed to authorize it, or has forbidden it, no amount of acquiescence or consent or approval of the doing it by a ministerial officer, can create a right to do the thing which is unauthorized or forbidden * * * . The insurance department had no power to authorize or acquiesce in the issuance of policies unauthorized or forbidden by statute." Dept. of Ins. vs. Church, etc., 217 Ind. 58, 26 N. E. 2d 51, 128 A.L.R. 635.
>
> 4. " * * * Life insurance contracts are so important in our modern life and affect so many persons of all

classes, including widows and orphans, and are so beneficial in their effects, that they may well receive the consideration and protection of the lawmaking powers. If, therefore, that power has spoken and has regulated the matter of insurance contracts, and has undertaken to prevent fraud and misrepresentation so far as possible for the protection of the insured, and all those who contemplate entering into insurance contracts, it is the solemn duty of the Courts to enforce the provisions of the statute when called on to do so." Ut. Ass'n of Underwriters, supra, 200 Pac. 675.

V

IN SUPPORT OF THE FOUR GENERAL POINTS DISCUSSED HEREIN WE PRESENT THE FOLLOWING STATUTES AND AUTHORITIES SHOWING THAT PLAINTIFFS ARE ENTITLED TO THE RETURN OF THEIR PREMIUMS:

1. "An insurance contract which has the effect of furthering any matter or thing prohibited by statute, falls within the same rule as contracts generally and is therefore void." Bridwell vs. Tri State Ins. Co., 286 Pac. 2d 736, 740, Decided (Okla.) July 19, 1955.

2. The usual test applied by Courts in determining whether a contract offends public policy and is antagonistic to the public interst is whether the contract has a tendency toward such an evil. Wood vs. Casserleigh, 30 Colo. 287, 71 Pac. 360; if it is opposed to the interest of the public, or has a tendency to offend public policy, it will be declared invalid, even though the parties acted in good faith and no injury to the public would result in the particular instance;" Stearns, vs. Williams (Idaho) 240 Pac. 2d 833, 837.

3. Within the intent of this code the business of insurance is one affected with a public interest, requiring that all persons be actuated by good faith, abstain from deception, and practice equity in all insurance matters. Upon the insurer, the insured and their representatives rests the duty of preserving inviolate the integrity of insurance." Section 31-1-8, P.C.A. 1953.

4. "Violation of any provision of this code shall be a misdemeanor, unless otherwise provided in this code." Section 31-1-6, U.C.A. 1953.

5. "The legislature can prohibit the formation of any bargain and thereby make it illegal. The question whether the legislature has done so depends on interpretation of legislative action. In case of *express prohibition* or of *declaring the act a crime,* there can be no doubt." Restatement of Contracts, Volume II, Page 1088, Comments.

6. "A policy of insurance may be void ab initio * * * for illegality, the parties not being in pari delecto; * * * in all such cases the premium is returnable * * * . It has also been said that if the policy is invalid and the insured was guilty of no fraud in procuring it, the premium is returnable." 3 Couch on Insurance 2353, Sec. 710.

7. "(1) It is manifest that the statute was enacted for the protection of those who are solicited to enter into life insurance contracts who may lack the experience and the opportunity to guard themselves against the evils of the experienced life insurance solicitor." Mountain States Life case supra.

VI

CONCLUSION

We respectfully submit that the Complaint in this case states ample facts to constitute a compensable claim, and in connection with the proof offered in support thereof there is sufficient to support a judgment for the return of all premiums to the Plaintiffs herein, as prayed.

WHEREFORE: Plaintiffs pray that the judgment of the lower court be reversed and judgment be entered in favor of Plaintiffs.

Respectfully submitted,

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